FILE COPY

Office - Supreme Court, U. S.
FILED
JUN 30 1939
CHARLES ELMORE CROPLEY
CLERK

No. 49

In the Supreme Court of the United States

OCTOBER TERM, 1939

GEORGE W. GRIFFITHS, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statute involved	2
Statement	4
Summary of argument	7
Argument:	
The transaction did not constitute an installment sale within the meaning of the statute and the taxpayer must be treated as having received the full profit in 1933	9
Conclusion	24

CITATIONS

Cases:

Ahles Realty Corp. v. *Commissioner*, 71 F. (2d) 150, certiorari denied, 293 U. S. 611	16
Askin & Marine Co. v. *Commissioner*, 66 F. (2d) 776	9
Bassick v. *Commissioner*, 85 F. (2d) 8, certiorari denied, 299 U. S. 592	16
Blum's, Incorporated v. *Commissioner*, 17 B. T. A. 386	11
Bogardus v. *Commissioner*, 302 U. S. 34	22
Burnet v. *Leininger*, 285 U. S. 136	13
Burnet v. *Sanford & Brooks Co.*, 282 U. S. 359	9
Chisholm v. *Commissioner*, 79 F. (2d) 14, certiorari denied, 296 U. S. 641	20
Commissioner v. *Ashland Oil & R. Co.*, 99 F. (2d) 588, certiorari denied, April 17, 1939, Nos. 692, 693, 757, 758, 1938 Term	16
Commissioner v. *Liberty Bank & Trust Co.*, 59 F. (2d) 320	9
Commissioner v. *Schumacher Wall Bd. Corp.*, 93 F. (2d) 79	16
Douglas v. *Willcuts*, 296 U. S. 1	23
Electrical Securities Corp. v. *Commissioner*, 92 F. (2d) 593	16, 20
First Seattle D. H. Nat. Bank v. *Commissioner*, 77 F. (2d) 45	16
Gregory v. *Helvering*, 293 U. S. 465	8, 11, 12, 13, 15, 16, 20, 21
Groves v. *Commissioner*, 99 F. (2d) 179	18
Hazeltine Corp. v. *Commissioner*, 89 F. (2d) 513	16
Helvering v. *Amer. Chicle Co.*, 291 U. S. 426	23
Helvering v. *Bashford*, 302 U. S. 454	15
Helvering v. *Elkhorn Coal Co.*, 95 F. (2d) 732, certiorari denied, 305 U. S. 605, rehearing denied, 305 U. S. 670	16, 20

189446—39——1

Cases—Continued. Page

Helvering v. *Gordon*, 87 F. (2d) 663 19
Helvering v. *Gregory*, 69 F. (2d) 809, reversing 27 B. T. A. 223, aff'd, 293 U. S. 465 21
Helvering v. *Intermountain Insurance Co.*, 294 U. S. 686 ... 11
Helvering v. *Minnesota Tea Co.*, 89 F. (2d) 711, reversing 34 B. T. A. 145, aff'd, 302 U. S. 609 22
Helvering v. *Rankin*, 295 U. S. 123 22
Helvering v. *Tex-Penn Co.*, 300 U. S. 481 22
Higgins v. *Smith*, No. 146, 1939 Term 17
Jackson v. *Commissioner*, 39 B. T. A. 937 18
Loewenberg v. *Commissioner*, 39 B. T. A. 844 ..... 17, 21
Lucas v. *Earl*, 281 U. S. 111 13
Marine Transport Co. v. *Commissioner*, 77 F. (2d) 177 9
McInerney v. *Commissioner*, 82 F. (2d) 665 20
Miller v. *Commissioner*, 103 F. (2d) 58 16
Minnesota Tea Co. v. *Helvering*, 302 U. S. 609 ..... 13, 20, 22
Old Colony Tr. Co. v. *Commissioner*, 279 U. S. 716 22
Prairie Oil & Gas Co. v. *Motter*, 66 F. (2d) 309 16
Putnam Nat. Bank v. *Commissioner*, 50 F. (2d) 158 9
S. A. MacQueen Co. v. *Commissioner*, 67 F. (2d) 857 19
Starr v. *Commissioner*, 82 F. (2d) 964, certiorari denied, 298 U. S. 680 16
Thurber v. *Commissioner*, 84 F. (2d) 815 16
United States v. *Boston & M. R. Co.*, 279 U. S. 732 23
United States v. *Hendler*, 303 U. S. 564 23
United States v. *Kirby Lumber Co.*, 284 U. S. 1 23
Von's Investment Co., Ltd. v. *Commissioner*, 39 B. T. A. 1141 18
West Texas Refining & D. Co. v. *Commissioner*, 68 F. (2d) 77 16

Statutes:

Revenue Act of 1926, c. 27, 44 Stat. 9, Sec. 212 11
Revenue Act of 1932, c. 209, 47 Stat. 169:
Sec. 22 2
Sec. 44 (a) 3
Sec. 44 (b) 3, 10
Revenue Acts of 1928, 1932, 1934, 1936, and 1938, Sec. 44 ... 11

Miscellaneous:

1 Paul & Mertens, *Law of Federal Income Taxation* (1934), §12.01 11
Treasury Regulations 33, Art. 117 11

In the Supreme Court of the United States

OCTOBER TERM, 1939

No. 49

GEORGE W. GRIFFITHS, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 60–70) is reported in 37 B. T. A. 314. The opinion of the Circuit Court of Appeals (R. 84–91) is reported in 103 F. (2d) 110.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered February 25, 1939 (R. 91). A petition for rehearing was denied on April 15, 1939 (R. 92). The petition for certiorari was filed May 10, 1939, and was granted October 9, 1939. The jurisdiction of

this Court is conferred by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The taxpayer in 1926 purchased securities for $100,000 which he sold in 1931 for $7,500, and was allowed a deductible loss in the amount of the difference. He subsequently learned of fraud in the original sale, and in 1933 was about to conclude a favorable settlement with his vendor, whereby the vendor would repurchase these securities for $100,000. In contemplation of the settlement the taxpayer reacquired the securities for $8,000. In order to avoid the income taxes that would accrue immediately against him with respect to the profit on the settlement, he organized a wholly owned corporation, and purported to sell the securities to that corporation on the installment plan, payments to be spread over a period of forty years. He then concluded the settlement with his original vendor, releasing him of all claims, but without revealing that he was purporting to act for an undisclosed principal, his corporation.

The question presented is whether he is taxable upon the profit realized from that settlement, or whether the interposition of the wholly owned corporation effectively precludes the tax.

STATUTE INVOLVED

Revenue Act of 1932, c. 209, 47 Stat. 169:

> SEC. 22. GROSS INCOME.
>
> (*a*) *General Definition.*—"Gross income" includes gains, profits, and income derived from

salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

SEC. 44. INSTALLMENT BASIS.

(a) *Dealers in Personal Property.*—Under regulations prescribed by the Commissioner with the approval of the Secretary, a person who regularly sells or otherwise disposes of personal property on the installment plan may return as income therefrom in any taxable year that proportion of the installment payments actually received in that year which the gross profit realized or to be realized when payment is completed, bears to the total contract price.

(b) *Sales of Realty and Casual Sales of Personalty.*—In the case (1) of a casual sale or other casual disposition of personal property (other than property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year), for a price exceeding $1,000, or (2) of a sale or other disposition of real property, if in either case the initial payments do not exceed 40 per centum of the selling price, the income may, under regulations prescribed by the Commissioner with the approval of the Secretary, be returned on the

basis and in the manner above prescribed in this section. As used in this section the term "initial payments" means the payments received in cash or property other than evidences of indebtedness of the purchaser during the taxable period in which the sale or other disposition is made.

STATEMENT

The facts, as found by the Board (R. 60–65), may be stated as follows:

In 1926, taxpayer purchased from or through Robert D. Bay at a cost of $100,000, 5,000 shares of the capital stock of the Oakridge Cemetery Corporation. On October 30, 1931, he sold those shares to the John Griffiths Investment Trust for $7,500.[1] For the year 1931, taxpayer, in his income tax return, claimed and was allowed a deduction of $92,500, as a loss from these transactions (R. 60–61).

Taxpayer, late in 1932, discovered that Lay had probably defrauded him in the 1926 purchase of the shares in question. He consulted Harry Markheim, an attorney, who investigated and commenced negotiations to bring about a settlement. On January 9, 1933, taxpayer was advised by Markheim that Lay would probably enter into a settlement, which was to take the form of a repurchase of the shares by Lay for $100,000 (R. 61). Taxpayer on the following

[1] It further appears that shortly thereafter, on November 16, 1931, he repurchased those shares for $7,000, and again sold them to the same purchaser for $7,000 on December 30, 1931 (R. 60–61). However, nothing appears to turn upon that repurchase and resale.

day reacquired that stock for that purpose paying $8,000 therefor (R. 61).

Markheim at the same time informed the taxpayer that he might effect a postponement of the time of payment of the income taxes on the profit arising from the settlement and that he might also reduce the amount of tax by organizing an "investment company" to which he would sell the stock on the installment basis, permitting the investment company to make the settlement with Lay. Taxpayer had theretofore given thought to the formation of an investment corporation. On January 9, 1933, he instructed Markheim to organize an "investment corporation" as Markheim had suggested (R. 61).

Accordingly, arrangements were made on January 10, 1933, through the Corporation Trust Company, for the organization of the G. W. G. Corporation under the laws of Delaware, with three of Markheim's associates as directors (R. 61–62). The taxpayer at the same time paid $1,000 for all of its capital stock, which he still holds (R. 62).

On the same day, the taxpayer sold to G. W. G. the Oakridge Cemetery Corporation stock (which he had just reacquired on that same day) together with any rights that he might have "to require said Robert D. Lay to purchase said stock" (R. 61–62). In consideration therefor G. W. G. agreed (1) to pay him $85,000, over a period of forty years,[2]

[2] Payment was to be made, $1,000 immediately, $1,125 on January 15, 1933, and $2,125 on each January 15 thereafter until fully paid (R. 62).

and (2) to pay 15% of the net amount received from Lay to one E. H. Harrison in discharge of the taxpayer's obligation to Harrison (R. 62).

On January 11, 1933, the directors of the G. W. G. Corporation approved the sale of the Cemetery Corporation stock to Lay for $100,000 and authorized taxpayer "either in his own name or in the name of the corporation" to do whatever might be necessary or desirable to consummate the sale. Taxpayer, as treasurer of the corporation, was also authorized to invest the proceeds of the sale (R. 63).

The settlement with Lay was concluded on January 11, 1933, whereby Lay gave two checks payable to the taxpayer, one for $100,000, and the other for $80,000 in connection with other matters not here in dispute. The taxpayer transferred the Cemetery Corporation stock to Lay, and for himself, his heirs, and assigns, released Lay of all claims, etc., which the taxpayer or his assigns might have against him (R. 63–64). It does not appear that Lay or his attorneys knew of the taxpayer's prior sale to G. W. G., or that he was acting for G. W. G. as his undisclosed principal (R. 66).

The $100,000 check was endorsed by the taxpayer and deposited on January 12, 1933 in the bank account of G. W. G. (R. 64).

In accordance with the terms of the agreement between the taxpayer and G. W. G., he received $1,000 and $1,125 from it in 1933, although payments were made in March rather than in January, as

originally stipulated (R. 64). In addition he received $1,243.13 from G. W. G. in December 1933, as interest on the unpaid portion of the purchase price (R. 64).

In his income tax return for 1933, the taxpayer reported no income on account of his transaction with Lay, but he did report the sum of $1,875 which he treated as the profit embodied in the $2,125 installments received from G. W. G. during that year (R. 64–65).

The Commissioner rejected the purported installment sale of the stock by the taxpayer to G. W. G., and proposed to assess a deficiency computed by treating the transaction as a direct sale by the taxpayer to Lay and by including in the taxpayer's gross income the full profit realized upon that sale. The Board of Tax Appeals (six members dissenting) overruled the Commissioner, but the Circuit Court of Appeals reversed the Board.

SUMMARY OF ARGUMENT

1. This case presents an attempt artificially to convert a cash sale into an installment sale by introducing a dummy corporation as an intermediary, all for the purpose of tax avoidance. The corporation was wholly owned by the taxpayer and was created overnight with directors supplied from among the office associates of the taxpayer's counsel. It was at most a mere collection and remittance agency for the purpose of this transaction.

It is our position that the installment sales provisions were never meant by Congress to be applicable in a situation of this kind. Like the corporate reorganization provisions, the installment sales provisions are remedial in character, and were never intended to implement tax avoidance. They should be held inapplicable here just as the corporate reorganization provisions were held inapplicable in *Gregory* v. *Helvering*, 293 U. S. 465, where a ritualistic compliance with the literal language of the statute was nevertheless ruled to be beyond its scope. As it did in that case, the Court here should also look to what was actually done, and the substance of the present transaction consists of nothing more than a mere sale for $100,000 cash, the profit on which should immediately be subject to tax.

2. The question involved is not one of fact, but depends upon the legal consequences which flow from the facts. The Circuit Court of Appeals was therefore justified as a matter of law in reversing the Board. The *Gregory* case itself appeared in the same posture. The Board had ruled against the Government and the Circuit Court of Appeals reversed. Both the Circuit Court of Appeals and this Court treated the issue as one of law. We are here asking the Court to apply the principle of the *Gregory* decision to the present case, and if it is applicable, the scope of review should be the same.

3. An additional ground for supporting the decision of the court below may be found in the two-

fold consideration that the taxpayer in 1933 received taxable income (a) to the extent that his corporation discharged his obligation to E. H. Harrison, and (b) to the extent that he received the promise of his corporation to pay him $85,000, a promise that was backed dollar for dollar by cash over which he could exercise complete control.

ARGUMENT

THE TRANSACTION DID NOT CONSTITUTE AN INSTALLMENT SALE WITHIN THE MEANING OF THE STATUTE AND THE TAXPAYER MUST BE TREATED AS HAVING RECEIVED THE FULL PROFIT IN 1933.

1. This case presents an attempt by the taxpayer to postpone or avoid taxation by artificially converting a simple cash sale into an installment sale through the use of a wholly owned intermediary corporation created for that purpose. Had he sold the stock directly to Lay for $100,000 the full profit would immediately have become taxable to him.[3]

In order to avoid the immediate incidence of that tax, he undertook to route the sale to Lay through the newly organized G. W. G. Corporation, and

[3] That the profit realized would be taxable is clear. He had already had the advantage of a $92,500 deduction in 1931, and the recoupment of losses, etc., previously deducted in computing net income in earlier years, constitutes taxable income. Cf. *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359; *Commissioner* v. *Liberty Bank & Trust Co.*, 59 F. (2d) 320 (C. C. A. 6th); *Askin & Marine Co.* v. *Commissioner*, 66 F. (2d) 776 (C. C. A. 2d); *Putnam Nat. Bank* v. *Commissioner*, 50 F. (2d) 158 (C. C. A. 5th); *Marine Transport Co.* v. *Commissioner*, 77 F. (2d) 177, 179 (C. C. A. 5th).

went through the form of first making an installment sale of the stock to G. W. G. Thus, if he were successful in his scheme he could, by relying upon Section 44 (b) of the Revenue Act of 1932, spread the profit over a period of forty years. He would therefore achieve not only a postponement of tax, but would also actually reduce the aggregate amount of tax by removing the profit from the higher brackets and spreading it thinly over the years in lower brackets.

The Commissioner of Internal Revenue, ignoring the alleged assignment to G. W. G., treated the transaction simply as a sale by the taxpayer to Lay, and proposed to assess a deficiency by including the full profit in the taxpayer's gross income. We respectfully submit that the Commissioner was correct, and that the provisions for spreading the profit on installment sales in Section 44 (b) were never intended to apply to such an empty ritual as the taxpayer attempted to stage here.

The installment-sales provisions are remedial in character. They constitute a departure from the two principal systems of accounting, cash and accrual, and were designed to alleviate hardships to taxpayers by treating each payment partly as a return of capital and partly as gain, thus preventing the lumping of the profit in a single year in

disproportionately high surtax brackets.[4] But, as has been stated in 1 Paul and Mertens, *Law of Federal Income Taxation* (1934), § 12.01:

> It should be kept in mind that these provisions [installment sales] are of a relief character and accordingly the construction to be given them must be of a strict nature and against the party seeking relief.

See *Blum's, Incorporated* v. *Commissioner*, 17 B. T. A. 386, 389. Cf. *Helvering* v. *Inter-mountain Insurance Co.*, 294 U. S. 686, 689.

It is our position that the installment sales provisions were not intended to apply to such a situation as is presented here, just as the corporate reorganization provisions were held inapplicable in *Gregory* v. *Helvering*, 293 U. S. 465. In the *Gregory* case, the taxpayer's wholly owned corporation transferred securities to a new corporation, organized to avoid taxes, which issued all its shares to the taxpayer, and which was subsequently dissolved and liquidated by the distribution of the securities to the taxpayer.

[4] Prior to 1926, the Revenue Acts specifically recognized only two systems of accounting for reporting income, cash and accrual. Where sales were made on the installment plan, the application of either of these systems often led to hardship. The Commissioner sought to offer some relief through regulations, the first of which appeared in the 1918 edition of Regulations 33, Article 117. In 1926, Congress expressly recognized and approved this method. Section 212 (d) of the Revenue Act of 1926. And like provisions have appeared with some modification from time to time in all of the succeeding Revenue Acts. Section 44 of the Revenue Acts of 1928, 1932, 1934, 1936, and 1938.

The Court held that although the transaction complied with the literal terms of the statute with respect to corporate reorganizations, nevertheless it was not entitled to the exemption from tax that those provisions were intended to confer. The absence of any business purpose in the transaction placed it outside the scope of the statutory provisions. The Court looked to the substance of the situation, and concluded that the use of the specially organized corporation was but (p. 469)—

> an operation having no business or corporate purpose—a mere device which put on the form of a corporate reorganization as a disguise for concealing its real character, and the sole object and accomplishment of which was the consummation of a preconceived plan, not to reorganize a business or any part of a business, but to transfer a parcel of corporate shares to the petitioner.

Similarly here, the creation of G. W. G. and the installment sale to it were but steps in the consummation of the preconceived plan of transferring the stock to Lay for $100,000. And just as the Court refused to apply the reorganization provisions in the *Gregory* case to a situation which they literally covered, so here the court below correctly refused to apply the installment sales provisions to the case at bar. In both, the particular provisions were remedial in character and never intended by Congress to be vehicles for tax avoidance. Here, as in the *Gregory* case, this Court is entitled to look to the substance

of what was done. The installment sale to G. W. G. followed by the use of G. W. G. as a reservoir for the money received from Lay to be syphoned out periodically by the taxpayer, and meanwhile subject to his plenary control, is indeed as transparent and meaningless a device as was unsuccessfully employed in the *Gregory* case. The same principles which governed the *Gregory* decision are likewise applicable here.[5]

The doctrine of the *Gregory* case was applied and extended in *Minnesota Tea Co.* v. *Helvering*, 302 U. S. 609, where it was necessary to determine whether there had been, within the meaning of the statute, a "distribution" of cash by a corporation to its stockholders which it had received in a corporate reorganization. Any otherwise taxable gain to the corporation embodied in that cash would be exempt to the extent that it was "distributed" to the stockholders. The corporation in fact had distributed such cash to its stockholders on condition that they pay it over to creditors of the corporation in discharge of its debts. Thus, there was literally a "distribution" to stockholders, but this Court held, applying the *Gregory* case, that the transaction really amounted to nothing more than a payment to creditors, rather

[5] The principle of the *Gregory* case is particularly applicable here in view of the fact that the income had already accrued in the taxpayer's favor, and the device employed was merely an anticipatory attempt to deflect that income for tax purposes. Cf. *Burnet* v. *Leininger*, 285 U. S. 136; *Lucas* v. *Earl*, 281 U. S. 111.

than a "distribution" to stockholders. It denied the exemption, saying (pp. 613–614):

> Payment of indebtedness, and not distribution of dividends, was, from the beginning, the aim of the understanding with the stockholders and was the end accomplished by carrying that understanding into effect. A given result at the end of a straight path is not made a different result because reached by following a devious path. The preliminary distribution to the stockholders was a meaningless and unnecessary incident in the transmission of the fund to the creditors, all along intended to come to their hands, so transparently artificial that further discussion would be a needless waste of time. The relation of the stockholders to the matter was that of a mere conduit. The controlling principle will be found in *Gregory* v. *Helvering*, 293 U. S. 465, 469–470; * * *.

Applying those principles here, the taxpayer simply made a sale to Lay for $100,000, and he should be subject to the tax consequences which flow from that transaction. The interposition of G. W. G., his *alter ego*, could not change the essential character of the transaction. G. W. G. was merely a conduit. It was created on the eve of the settlement with Lay, and its directors were supplied from among the office associates of taxpayer's counsel. Its function in this transaction was at most simply that of a collection and remittance agency. It certainly was not buying stock on the installment plan. Lay was the one who was buying the stock, and he paid cash.

G. W. G. had no assets other than the $1,000 capital paid in by the taxpayer, and yet it agreed to buy the cemetery stock from him for $85,000. It was merely to hold the stock for a very short time and then pass it on to Lay. In fact the agreement between the taxpayer and G. W. G. refers to the sale of the stock to Lay, which had undoubtedly been arranged, though not finally consummated, the day before G. W. G. was created. It was contemplated from the beginning that G. W. G. was merely to collect the $100,000, pay about $15,000 thereof to a third party (E. H. Harrison) in discharge of the taxpayer's obligation to him, and to pay the remaining $85,000 periodically to the taxpayer, who meanwhile would exercise plenary control over the investment of the fund and who could at any time use it for any purpose he might choose. We submit that the Court is entitled as a matter of law to look at the substance of this transaction and treat it simply as a sale by the taxpayer to Lay, disregarding the attempted application of the installment sales provisions as outside the scope of the statute, just as the Court held the transactions in the *Gregory* case outside the scope of the reorganization provisions and looked to the essential character of the transaction there presented.

Here, as in *Helvering* v. *Bashford*, 302 U. S. 454, 458, the ownership of the stock by the intermediary corporation "was transitory and without real substance; it was part of a plan which contemplated the immediate transfer of the stock". And the same principle has been applied in a wide variety of cases

holding that a transaction carried out in accordance with a preconceived plan may not be split up into its component parts, and that the substance rather than the form of the transaction must control. See *Helvering* v. *Elkhorn Coal Co.*, 95 F. (2d) 732 (C. C. A. 4th), certiorari denied, 305 U. S. 605, rehearing denied, 305 U. S. 670; *Electrical Securities Corp.* v. *Commissioner*, 92 F. (2d) 593 (C. C. A. 2d); *Starr* v. *Commissioner*, 82 F. (2d) 964 (C. C. A. 4th), certiorari denied, 298 U. S. 680; *Bassick* v. *Commissioner*, 85 F. (2d) 8, 10 (C. C. A. 2d), certiorari denied, 299 U. S. 592, rehearing denied, 299 U. S. 623; *Hazelline Corp.* v. *Commissioner*, 89 F. (2d) 513 (C. C. A. 3d); *Commissioner* v. *Schumacher Wall Bd. Corp.*, 93 F. (2d) 79 (C. C. A. 9th); *Miller* v. *Commissioner*, 103 F. (2d) 58 (C. C. A. 6th); *Commissioner* v. *Ashland Oil & R. Co.*, 99 F. (2d) 588, 591 (C. C. A. 6th), certiorari denied, April 17, 1939, Nos. 692, 693, 757, 758, 1938 Term; *First Seattle D. H. Nat. Bank* v. *Commissioner*, 77 F. (2d) 45 (C. C. A. 9th); *Thurber* v. *Commissioner*, 84 F. (2d) 815, 818 (C. C. A. 1st); *Ahles Realty Corp.* v. *Commissioner*, 71 F. (2d) 150, 151 (C. C. A. 2d), certiorari denied, 293 U. S. 611; *Prairie Oil & Gas Co.* v. *Motter*, 66 F. (2d) 309, 311 (C. C. A. 10th); *West Texas Refining & D. Co.* v. *Commissioner*, 68 F. (2d) 77, 79–80 (C. C. A. 10th).

Nor is the principle of the *Gregory* case to be limited to cases dealing with corporate reorganizations, as indicated by the Board of Tax Appeals (R. 67). There is nothing in the statute which

even suggests that a realistic approach must be reserved exclusively for reorganization cases. We have discussed this matter at length in our brief in *Higgins* v. *Smith*, No. 146, to be argued immediately after the present case, and we there called attention (p. 26) to the impressive number and range of cases outside the field of reorganizations that have treated the principle of the *Gregory* case as applicable.

Moreover, in a subsequent case substantially identical with the case at bar (*Loewenberg* v. *Commissioner*, 39 B. T. A. 844), the Board of Tax Appeals itself has receded from the position taken by the majority of its members in the instant case. It referred at length with apparent approval to the opinion of the court below in the instant case, and concluded (pp. 851–852):

> This petitioner, like Griffiths, sold her stock upon the installment basis to a corporation created about 24 hours before the time of sale, with the definite intention and upon the advice of counsel that such an arrangement might postpone or limit the amount of her income taxes. Like the corporation organized by Griffiths, Malvina was created for the stated purpose of an investment company, but this petitioner would further justify the existence of Malvina by attempting to show that other considerations entered into its creation. We are not persuaded by petitioner's argument, nor by the elaborate minutes of Malvina, that such corporation was anything more than a contrivance intention-

ally created for the sole purpose of enabling the taxpayer to avoid a tax which would otherwise be due the Government.

In our opinion the real purpose in creating Malvina was to route through it the transfer of stock that petitioner had agreed to sell to Golo, and thus deflect from her the tax upon the income she would have received during the taxable year but for the intervening transfer on the installment basis to Malvina. Malvina's receipt of the purchase price of the stock from Golo, investment of the proceeds, and payment of the installment obligations as they matured were but incidental to the real purpose for which it was created. To permit a taxpayer thus to circumvent the tax laws and escape a tax which Congress plainly intended to impose would exalt artifice above reality and deprive the statutory provisions of all serious purpose. We, therefore, sustain the respondent's determination.

And shortly thereafter a unanimous Board applied the same principles in a closely analogous situation where the taxpayer had attempted to use a wholly owned corporation as the vehicle for selling certain securities owned by him. *Jackson* v. *Commissioner*, 39 B. T. A. 937. Cf. *Von's Investment Co., Ltd.* v. *Commissioner*, 39 B. T. A. 1141, 1144.

In *Groves* v. *Commissioner*, 99 F. (2d) 179 (C. C. A. 4th), the court refused to permit a taxpayer to

escape a tax upon otherwise taxable income by organizing two corporations owned and controlled by him in anticipation of diverting to them the income he knew he would receive. The court characterized the transactions as an anticipatory arrangement for the deflection of income and concluded that they must be disregarded for purposes of taxation. There, as here, the Circuit Court of Appeals disregarded the fact that the money was left with the corporation, in that case at least through the period of litigation. The concluding remarks of the court are particularly pertinent here (p. 183):

> The various steps taken by the petitioner were anticipatory arrangements for the deflection of income. The Wagegro and Firinbank Corporations were not created by the petitioner for the purpose of carrying on any real or actual business in the ordinary way but only in furtherance of the scheme to evade taxation. The Board was justified in looking through the form to the substance of the various transactions arranged and carried out by the petitioner. The petitioner in effect received and still enjoys the possession of the proceeds of the sale of the 23,000 shares of the Securities stock and should be taxed for the $575,000 as income for the year 1930.

Compare *Helvering* v. *Gordon*, 87 F. (2d) 663 (C. C. A. 8th); *S. A. MacQueen Co.* v. *Commissioner*, 67 F.

(2d) 857 (C. C. A. 3d); *McInerney* v. *Commissioner*, 82 F. (2d) 665 (C. C. A. 6th).[6]

[6] The petitioner places considerable reliance upon *Chisholm* v. *Commissioner*, 79 F. (2d) 14 (C. C. A. 2d), certiorari denied, 296 U. S. 641, where a partnership was created and employed by its members for tax avoidance purposes. However, the Circuit Court of Appeals there treated the partnership as having been organized for the purpose, in addition, of exercising normal business functions, and thus distinguished the *Gregory* case. We believe that the court in the *Chisholm* case erred in so confining the *Gregory* decision. It should be sufficient that the particular transaction has no business purpose, and it should not matter that the partnership or wholly owned corporation otherwise has a business purpose, if the particular transaction involved is wholly lacking in reality or business purpose. Thus in *Minnesota Tea Co.* v. *Helvering*, 302 U. S. 609 and in *Helvering* v. *Elkhorn Coal Co.*, 95 F. (2d) 732 (C. C. A. 4th), *supra*, there were transactions related to ultimate business objectives, but the essential element in both was the lack of any such business objective in the particular form in which the transactions were cast. The Second Circuit, however, has failed to give full play to the *Gregory* decision and unduly restricted it in the *Chisholm* case as it likewise did in an extended dictum in *Electrical Securities Corp.* v. *Commissioner*, 92 F. (2d) 593, 595 (bottom of first column) where the very situation there discussed and stated to be outside the scope of the *Gregory* case was later held to be within the doctrine of the *Gregory* case in *Helvering* v. *Elkhorn Coal Co.*, *supra*.

But even if the *Chisholm* case be accepted as good law, it is nevertheless distinguishable here. It was not shown in the present case that G. W. G. was ever employed for any purpose beyond the avoidance of the tax with respect to the profit on the Lay settlement. While it is true that it made several isolated purchases and sales of securities thereafter (R. 59), there is no showing or finding that the transactions constituted anything more than the investment and reinvestment of the money received from Lay, and that they were merely incidental to the safekeeping of those funds on behalf of the petitioner.

2. The taxpayer argues (Br. 18-23) that the facts found by the Board are conclusive if supported by substantial evidence. We do not disagree. But we do contend that whether the taxpayer is to be treated under the statute as having made the sale directly to Lay is a question of law or at least a mixed question of law and fact, to be determined upon the basis of the evidentiary facts. The Board itself regards this as a question of law, for in *Loewenberg* v. *Commissioner*, 39 B. T. A. 844, where it rejected the result it had reached in the instant case, it treated the issue as one of law, and in particular of the applicability of the principle of the *Gregory* case.

Indeed the *Gregory* case itself plainly shows that the issue is one of law. In that case the Board had decided against the Government. *Gregory* v. *Commissioner*, 27 B. T. A. 223. Upon appeal, the Circuit Court of Appeals reversed. *Helvering* v. *Gregory*, 69 F. (2d) 809 (C. C. A. 2d). Had the issue been merely one of fact, the Circuit Court of Appeals would not have had any power to reverse, if the findings were supported by substantial evidence. However, neither the Circuit Court of Appeals nor this Court treated the case as turning upon the sufficiency of the evidence to support the findings. We submit that the question here is like that presented in the *Gregory* case and that the scope of review is the same.

Similarly the question in *Minnesota Tea Co.* v. *Helvering*, 302 U. S. 609, was regarded as one of law rather than of fact. The Board of Tax Appeals had there, too, ruled against the Commissioner. *Minnesota Tea Co.* v. *Commissioner*, 34 B. T. A. 145. The Circuit Court of Appeals reversed, *Helvering* v. *Minnesota Tea Co.*, 89 F. (2d) 711 (C. C. A. 8th), and this Court approved, treating the case as one involving the applicability of the doctrine of the *Gregory* case. Compare *Helvering* v. *Tex-Penn Co.*, 300 U. S. 481, 491; *Helvering* v. *Rankin*, 295 U. S. 123, 131; *Bogardus* v. *Commissioner*, 302 U. S. 34, 39.

3. The following is submitted as an additional ground for affirming the judgment below, a ground that does not require disregarding the corporate fiction, nor does it require treating the transaction as a sale by the taxpayer directly to Lay.

Taking the transaction on its face, it can be said that the taxpayer realized the full amount of profit in 1933, and that the installment sales provisions were not intended to relieve him of the obligation to report it as income for that year.

First. The payment of $14,566.08 by G. W. G. to E. H. Harrison in fulfillment of petitioner's debt to Harrison plainly represents income to petitioner, for it has already been firmly established that the discharge of an obligation constitutes income to the debtor. *Old Colony Tr. Co.* v. *Commissioner*, 279

U. S. 716; *United States* v. *Boston & M. R. Co.*, 279 U. S. 732; *Douglas* v. *Willcuts*, 296 U. S. 1, 9; *United States* v. *Hendler*, 303 U. S. 564, 566. Cf. *United States* v. *Kirby Lumber Co.*, 284 U. S. 1; *Helvering* v. *Amer. Chicle Co.*, 291 U. S. 426. Accordingly, that amount should have been reported by petitioner as income.

Second. He received a contractual promise by G. W. G. to pay him $85,000, with interest, and since that promise was backed by $85,000 in cash (immediately after the sale to Lay), which he was in a position to protect, he then received corporate paper that was obviously worth its face value. Except for the installment-sales provisions, that corporate paper embodied income that should have been reported in 1933.

It is therefore merely necessary to say that the installment-sales provisions were not intended to apply here, which we have already undertaken to establish in part 1, *supra*. For, if it be established that the installment-sales provisions are inapplicable, then even though full recognition be given to the existence and operations of G. W. G., there is taxable gain (the discharge of the obligation to Harrison plus the corporate paper) which petitioner must account for in 1933 but which he has not reported.

CONCLUSION

The decision of the court below is correct and should be affirmed.

Respectfully submitted.

ROBERT H. JACKSON,
Solicitor General.

SAMUEL O. CLARK, JR.,
Assistant Attorney General.

SEWALL KEY,
J. LOUIS MONARCH,
ARNOLD RAUM,
JOSEPH M. JONES,
Special Assistants to the Attorney General.

NOVEMBER 1939.

U. S. GOVERNMENT PRINTING OFFICE: 1939

SUPREME COURT OF THE UNITED STATES.

No. 49.—October Term, 1939.

George W. Griffiths, Petitioner,
vs.
Guy T. Helvering, Commissioner of Internal Revenue.

On Writ of Certiorari to the Circuit Court of Appeals for the Seventh Circuit.

[December 18, 1939.]

Mr. Justice Frankfurter delivered the opinion of the Court.

The case is here to review a decision of the Circuit Court of Appeals for the Seventh Circuit (103 F. (2d) 110) reversing an order of the Board of Tax Appeals (37 B. T. A. 314) which had overruled a deficiency assessment by the Commissioner of Internal Revenue in petitioner's income tax return for 1933. We granted *certiorari*, 308 U. S. —, because of an alleged conflict between the decision below and that of the Circuit Court of Appeals for the Second Circuit in *Smith* v. *Higgins*, 102 F. (2d) 456 (No. 146 this term).

The facts are undisputed, and, for purposes of our decision, may be thus abridged: In 1926 Griffiths, the petitioner, paid one Lay $100,000 for some stock. The investment was unprofitable, and the upshot of a complicated series of transactions was allowance to Griffiths by the Commissioner of a deductible loss of $92,500 for the year 1931 resulting from a sale of the stock by Griffiths to a family corporation. Thereafter, in 1932, Griffiths got wind of the fact that Lay had defrauded him in the 1926 sale. Negotiations were begun for a settlement of Griffiths' claim against Lay, and by January 1933, Griffiths' lawyer had devised an arrangement for such a settlement. The gist of the arrangement was this: Griffiths was to re-acquire the shares, convey them to a corporation newly created for the purpose of furthering the scheme and wholly controlled by Griffiths, which in turn was to transfer the stock back to Lay for $100,000 to be paid by him; and that sum was to be paid over by the corporation to Griffiths in annual installments for forty

years, with interest on the deferred payments.[1] The essentials of this scheme were carried out. Its purpose—to disguise by intervening elaborations what in fact was a rescission of the original purchase by Griffiths for $100,000—was made more manifest by these facts: Griffiths personally re-acquired and transferred the shares to Lay without revealing the existence of the new corporation, gave Lay a personal release of all claims against him, and personally received from Lay the $100,000 which he then turned over to the corporation.

On these findings the Commissioner ruled that Griffiths, having been allowed a deduction for loss attributable to the stock purchased from Lay and having now recouped that loss through settlement of his claim against Lay, was subject to tax for the amount of the settlement in 1933. We think the Commissioner was right, and that the Circuit Court of Appeals properly reversed the Board of Tax Appeals.

The facts leave little scope for legal explication. Griffiths had a claim for fraud against Lay which, when satisfied, wiped out the loss for which he had received an earlier deduction. Had satisfaction of the claim come to him without any conduit, it would have indisputably been his income. The claim having been recognized by Lay and cast into a form realizable by Griffiths, a lawyer's ingenuity devised a technically elegant arrangement whereby an intricate outward appearance was given to the simple sale from Griffiths to Lay and the passage of money from Lay to Griffiths. That was the crux of the business to Griffiths, and that is the crux of the business to us.

We cannot too often reiterate that "taxation is not so much concerned with the refinements of title as it is with actual command over the property taxed—the actual benefit for which the tax is paid." *Corliss* v. *Bowers*, 281 U. S. 376, 378. And it makes no difference that such "command" may be exercised through specific retention of legal title or the creation of a new equitable but controlled interest, or the maintenance of effective benefit through the

[1] Of the total sum paid, $15,000 was to be applied by the corporation in payment of a personal indebtedness owed by Griffiths. This sum, of course, was clearly income to petitioner. The remainder was to be paid in installments by the corporation to Griffiths. Petitioner contends that these installments alone are taxable to him as they are paid, under the provisions of § 44 of the Revenue Act of 1932, c. 209, 47 Stat. 169.

interposition of a subservient agency. Cf. *Gregory* v. *Helvering*, 293 U. S. 465. "A given result at the end of a straight path," this Court said in *Minnesota Tea Co.* v. *Helvering*, 302 U. S. 609, 613, "is not made a different result because reached by following a devious path." Legislative words are not inert, and derive vitality from the obvious purposes at which they are aimed, particularly in the provisions of a tax law like those governing installment sales in § 44 of the Revenue Act of 1932. Taxes cannot be escaped "by anticipatory arrangements and contracts however skilfully devised . . . by which the fruits are attributed to a different tree from that on which they grew." *Lucas* v. *Earl*, 281 U. S. 111, 115. What Lay gave, Griffiths in reality got, and on that he must be taxed. The judgment is

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.